

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE DEPARTMENT OF LABOR AND INDUSTRY

In the Matter of Midland Construction	FINDINGS OF FACT, CONCLUSIONS AND RECOMMENDATION
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The above-matter came on for a hearing before Administrative Law Judge Steve M. Mihalchick on August 23, 2006, at 9:00 a.m. at the Office of Administrative Hearings, 100 Washington Square, Suite 1700, Minneapolis, Minnesota. The hearing record closed at the conclusion of the hearing on August 23, 2006.

Michael J. Tostengard, Assistant Attorney General, 445 Minnesota Street, Suite 1200, St. Paul, MN 55101-2130, appeared on behalf of the Department of Labor and Industry.

Midland Construction and Ryan D. Reed were represented by William G. Peterson, 3601 Minnesota Drive, Suite 800, Bloomington, Minnesota, 55435.

STATEMENT OF ISSUES

1. Did Midland Construction engage in work of a residential building contractor after expiration of its license in violation of Minn. Stat. § 326.84, subds 1 and 1a?

The Administrative Law Judge (ALJ) concludes that the Midland Construction engaged in unlicensed residential building contractor activity.

2. Did Midland Construction engaged in fraudulent, deceptive or dishonest practice by failing to complete the contracted work on the Smoluch addition in violation of Minn. Stat. § 326.91, subd 1(2)?

The ALJ concludes that the Midland Construction violated Minn. Stat. Minn. Stat. § 326.91, subd 1(2) by failing to complete contracted-for work.

3. Did Midland Construction perform negligently or in breach of contract by failing to complete the contracted work on the Smoluch addition in violation of Minn. Stat. § 326.91, subd 1(4)?

The ALJ concludes that the Midland Construction has performed negligently or in breach of contract.

4. Did Midland Construction demonstrate financial irresponsibility by failing to pay an outstanding judgment in violation of Minn. Stat. § 326.91, subd. 1(6)?

The ALJ concludes that the Department has not demonstrated that Midland Construction demonstrated financial irresponsibility by failing to pay an outstanding judgment.

5. Does the personal bankruptcy of Ryan Reed, a general partner of Midland Construction, prevent the Department from taking action against Midland Construction?

The ALJ concludes that Ryan Reed's personal bankruptcy filing does not preclude the Department from taking action against Midland Construction.

Based upon all of the proceedings herein, the Administrative Law Judge makes the following:

FINDINGS OF FACT

1. Midland Construction (Midland) was licensed as a residential building contractor. According to Department records, Midland is a general partnership; 50% owned by Ryan Daniel Reed (Reed) and 50% owned by Frederick Young (Young).¹ Reed was Midland's "qualifying person." Midland's license terminated on March 31, 2004, when it was not renewed.²

2. The Department filed an amended complaint on April 21, 2006.³ Midland is the only party in this action and the Department is only seeking disciplinary action against it. Neither Reed nor Young are parties to this case and the Department does not seek an order against Reed or Young.⁴

3. On September 13, 2004, Reed, on behalf of Midland, entered into a written contract with Jon and Renee Smoluch to construct an addition to their home, including the installation of windows and exterior doors for \$11,500.⁵

4. Midland commenced work on the project on September 13, 2004, for which it requested and received \$5,900.⁶

¹ Testimony of Chris Williams, senior investigator for the Department.

² Testimony of C. Williams; Amended Statement of Charges.

³ Amended Statement of Charges

⁴ Statement of Michael J. Tostengard, Assistant Attorney General, representing the Department.

⁵ Ex. 2.

⁶ Amended Statement of Charges.

5. Midland ceased working on the addition. The work that had been performed was defective and the project was not completed.⁷

6. On November 29, 2004, the Smoluchs filed a claim in conciliation court in Hennepin County against Reed.⁸ The conciliation court case did not name Midland as a defendant.

7. On January 31, 2005 Reed filed a counter claim and mechanic's lien on the Smoluchs property in the amount of \$ 6,332.50.⁹

8. A conciliation court judgment was entered in favor of the Smoluchs in the amount of \$6,825.00 against Reed.¹⁰

9. On March 3, 2005, Reed had the conciliation court case removed to Hennepin County District Court.¹¹

10. On October 14, 2005, Reed filed a voluntary, individual Chapter 7 bankruptcy petition. Midland was not a party to the bankruptcy. Reed, the debtor, listed the Smoluchs as unsecured creditors with a claim of \$12,000.¹²

11. On November 10, 2005, the Hennepin County District Court entered judgment against Reed in favor of the Smoluchs.¹³ Midland was not a party in the District Court case.

12. On March 7, 2006, Renee Smoluch filed a complaint with the Department against "Ryan D. Reed, dba Midland Construction." The complaint stated that Ms. Smoluch was not requesting money or service, but wanted the Department to have a record of poor work and performance.¹⁴

13. The Bankruptcy Court entered a discharge of Reed's debts on March 23, 2006.¹⁵

14. The Smoluchs commenced an adversary proceeding in bankruptcy court to exempt the claim against Reed. The bankruptcy court ruled that the Hennepin County District Court judgment was void.¹⁶

⁷ Ex. 1.

⁸ Ex. 1.

⁹ Ex. 1.

¹⁰ Ex. 1.

¹¹ Ex. 1.

¹² Bankruptcy Petition, attached to Midland Construction's Motion.

¹³ Ex. 4.

¹⁴ Ex. 1.

¹⁵ Discharge of Debtor, attached to Midland Construction's Motion.

¹⁶ Notice of Bankruptcy Case Filing, attached to Midland Construction's Motion; Bankruptcy Petition, Schedule of Unsecured Creditors.

15. The Department filed a Notice of and Order for Hearing on March 28, 2006.¹⁷

16. On April 21, 2006, the Department filed an Amended Statement of Charges, which dismissed Young.¹⁸

17. On August 17, 2006, Reed filed a motion in this proceeding, seeking to stop the Department from taking action against Reed and Midland based on the alleged failure to pay a debt or to complete a contract because of the bankruptcy laws.¹⁹

Based upon the foregoing Findings of Fact, and for the reasons set forth in the attached Memorandum, the Administrative Law Judge makes the following:

CONCLUSIONS

1. The Commissioner of Labor and Industry and the Administrative Law Judge have jurisdiction in this matter under Minn. Stat. §§ 45.027, 326.91, and 14.50.

2. Midland was given timely and proper notice of the hearing in this matter.

3. The Department has complied with all procedural requirements of law.

4. The Department must prove by a preponderance of the evidence that the alleged violations occurred.²⁰

5. Minn. Stat. § 326.84, subds. 1 and 1a, require residential building contractors to be licensed. Residential building contractors may not perform work without a valid license. A residential building contractor is a person or entity that contracts to build or improve residential real estate by providing two or more special skills, including carpentry, masonry and concrete, interior finishing, exterior finishing, drywall and plaster.

6. By engaging in a contract to build an addition to a home after its residential building contractor's license expired, Midland engaged in unlicensed residential building contractor activities in violation of Minn. Stat. § 326.84, subds. 1 and 1a.

¹⁷ Notice of and Order for Hearing.

¹⁸ Amended Statement of Charges.

¹⁹ Motion of Ryan Reed, filed August 17, 2006.

²⁰ Minn. R. 1400.7300, subp. 5.

7. By failing to complete contracted-for work, Midland engaged in a fraudulent, deceptive or dishonest practice in violation of Minn. Stat. § 326.91, subd. 1(2).

8. By failing to complete contracted-for work, Midland performed negligently or in breach of contract in violation of Minn. Stat. § 326.91, subd. 1(4).

9. The Department has not shown Midland to be incompetent, untrustworthy and financially irresponsible in violation of Minn. Stat. § 326.91, subd 1(6). Midland was not sued. Reed alone was sued in Hennepin County District Court. Reed then filed for bankruptcy. The anti-discrimination provisions of the bankruptcy laws prohibit the Department from imposing sanctions against Reed for failing to pay a judgment that was declared void by the Bankruptcy Court.

10. Minnesota's residential contractor laws are a legitimate exercise of Minnesota's police power and the acts involved in this case are of the type the state has a legitimate interest in preventing.

11. The imposition of discipline and civil penalties against the Midland is in the public interest.

Based on the above Conclusions, the Administrative Law Judge makes the following:

RECOMMENDATION

IT IS RECOMMENDED that the Commissioner of Labor and Industry take disciplinary action and assess appropriate civil penalties against Midland Construction.

Dated: September 28, 2006

/s/ Steve M. Mihalchick
STEVE M, MIHALCHICK
Administrative Law Judge

Reported: Tape-Recorded (one tape);
No Transcript Prepared.

NOTICE

This report is a recommendation, not a final decision. The Commissioner of Labor and Industry will make the final decision after a review of the record. The Commissioner may adopt, reject or modify the Findings of Fact, Conclusions, and Recommended Decision. Under Minn. Stat. § 14.61, the final decision of the Commissioner shall not be made until this Report has been made available to the parties to the proceeding for at least ten days. An opportunity

must be afforded to each party adversely affected by this Report to file exceptions and present argument to the Commissioner. Parties should contact Nancy Leppink, Deputy Commissioner, Minnesota Department of Labor and Industry, 443 Lafayette Road North, St. Paul, MN 55155 to learn the procedure for filing exceptions or presenting argument.

If the Commissioner fails to issue a final decision within 90 days of the close of the record, this report will constitute the final agency decision under Minn. Stat. § 14.62, subd. 2a. In order to comply with this statute, the Commissioner must then return the record to the Administrative Law Judge within 10 working days to allow the Judge to determine the discipline to be imposed. The record closes upon the filing of exceptions to the report and the presentation of argument to the Commissioner, or upon the expiration of the deadline for doing so. The Commissioner must notify the parties and the Administrative Law Judge of the date on which the record closes.

Under Minn. Stat. § 14.62, subd. 1, the agency is required to serve its final decision upon each party and the Administrative Law Judge by first class mail or as otherwise provided by law.

MEMORANDUM

The record demonstrates that Midland violated statutes governing the conduct of residential building contractors. Midland contends that the bankruptcy filing of Reed, one of the two general partners and the person who signed the contract on behalf of Midland, prevents the Department from taking any action and entitles Reed to summary judgment or dismissal of the charges against him. The Department responds that Midland was not a party to the bankruptcy and that, in any event, the bankruptcy laws permit the Department to enforce licensing laws.

The Department concedes that Reed is not a party to this action and point out that the sole entity involved is Midland. Midland was not a party to the bankruptcy filing. The personal bankruptcy of Reed does not prohibit the Department from taking action against Midland because that entity was not a party to the bankruptcy proceedings.

Even if the bankruptcy filing affected or involved Midland, the bankruptcy code creates exceptions that authorize a state agency to enforce licensing laws despite bankruptcy.

The filing of a bankruptcy petition operates as a stay, applicable to all entities, of "the commencement or continuation... of a judicial, administrative, or other action or proceeding against the debtor..."²¹ An exception to the stay appears in section 362(b)(4) of the bankruptcy code for "the commencement or

²¹ 11 U.S.C. § 326(a)(1).

continuation of an action or proceeding by the governmental unit to enforce such governmental units' police or regulator powers."²²

Assuming the automatic stay was still in force when this proceeding was commenced, the Department's issuance of the Notice of and Order for Hearing falls within the ambit of section 362 (b)(4). Midland was charged with violation of Minnesota's residential contractor laws. The purpose of these laws is to guard the public against the consequences of incompetent workmanship and fraudulent conduct. The specific allegations involve unlicensed activity and misconduct and are of a type Minnesota has a legitimate interest in preventing. The bankruptcy case apparently concluded after the filing of the Notice of and Order for Hearing, but even if the automatic stay were an issue, section 362 (b)(4) permits the Department to take action regarding activities that violate the residential building contractor laws.

Section 524(a) of the bankruptcy code permanently enjoins all creditor actions to collect debts discharged under section 727. Section 727(b) provides in relevant part:

(b) Except as provided in section 523 of the title, a discharge under subsection (a) of this section discharges the debtor from all debts that arose before the date of the order for relief.

The permanent injunction of section 524(a) does not bar the Department from enforcing civil penalties for violations of Minnesota's residential contractor laws, nor does assessment of a civil financial penalty violate bankruptcy law. Section 523(a)(7) provides that a debt is not discharged "to the extent such debt is a fine, penalty or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss..."²³ The complaint by Ms. Smoluch expressly declines any request for personal compensation. Any civil penalty the Department may impose against Midland would be payable to the Department and would not be compensation for the Smoluchs' pecuniary loss.

For these reasons, the Department may take actions against Midland.

S.M.M.

²² 11 U.S.C. § 326(b)(4).

²³ 11 U.S.C. § 523(a)(7).